# Boosting Retirement Saving Across Europe

**Policy Brief**

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# Introduction

The need to boost retirement provision across the EU arises from the impact of demographic and economic change on most European countries. Most EU Member States have already embarked upon pensions reforms designed to increase retirement saving by individuals. The European Commission believes that a single pensions market across the continent can support this objective, but is also seeking to ensure the safety of private pensions saving (SEC(2010)830).

The first section of this paper looks at pensions reform throughout Europe, focusing on both the process of reform, the underlying causes, and the determinants of success.

The second section appraises the prospects for increasing retirement saving. It first establishes the importance of increased saving rates, before considering evidence on the determinants of savings behaviour, and the potential impact of the financial crisis.

The third section looks more closely at the EU's activities in this policy area and considers possible further steps.

On 18th June 2012, the ILC organised a private policy debate, hosted by the European Economic and Social Committee (EESC), supported by Prudential, and chaired by Mervyn Kohler of the Age Platform Social Protection Expert Group. The fourth section incorporates points raised on the day.

ILC are grateful to the following speakers for their input at the debate: Fritz von Nordheim (European Commission); Ria Oomen-Ruijten MEP (rapporteur of the European Parliament on the White Paper on Pensions); Xavier Verboven (EESC); Chris Verhaegen (Chair, EIOPA Occupational Pensions Stakeholder Group); Maureen O'Neill (EESC); and Mervyn Kohler (Age Platform Social Protection Expert Group).

# 1. Pensions reform throughout Europe

In the last decade many European countries have embarked upon reform of their pension systems. A variety of trends have been associated with this reform; as causal factors, principally the need to reduce burdens on public expenditure (and national solvency) resulting from the impact of demographic change on pension spending. Older societies reduce dependency ratios, meaning there are more retirees, living for longer, funded by a declining proportion of working-age citizens.

However, population ageing is not the only impetus behind reform. The process of economic globalisation – or more specifically, financialisation – has increased the pressure on the sustainability of traditional pensions provision, but also increased opportunities to establish new forms of private pensions provision. Europeanisation has increased pressure for harmonisation of pension provision, but also created opportunities, especially for accession countries, to modernise their pension systems as part of a wider transition to liberal democracy.

The general trend of post-industrialisation has affected pensions provision in Europe, by undermining the livelihoods and life-courses of individuals and the economic context within which pension entitlements are accrued. As David Natali argues:

The shift to a post-industrial employment structure has resulted in the presence in modern labour markets of new career profiles: part-time and interrupted careers for both sexes instead of the full-time continuous employment from an early age that was typical of the standard male worker… Yet the pension systems inherited from the post-war years are still clearly based on an industrial economy and labour market. Pension coverage, in most Western European countries, is optimal for workers who spend their entire working life in full-time employment. Part-time working usually results in reduced pension entitlements, as do career interruptions (Natali, 2008: 49).

The dynamic of post-industrialisation has therefore led all pensions systems in Europe to introduce flexibility in how pension entitlements are accrued.

Yet despite the apparent moves towards convergence across Europe, reform has been shaped by extant national-level institutions and practices (van Groezen et al, 2009). European pension systems are usually divided according to whether they represent 'Beveridgean' or 'Bismarckian' systems.

Beveridgean systems, named in honour of William Beveridge, the liberal thinker responsible for creating the blueprint for the UK welfare state in the 1940s, offer minimal levels of state pension provision (whether contributory or non-contributory), and expect any additional pension entitlements to be the product of private arrangements between employers and employees.

Bismarckian systems, named in honour of Otto von Bismarck, the formidable German politician responsible for introducing the earliest form of mass pension provision in the nineteenth century, blur the boundary between state and market by establishing state-backed pensions with compulsory employer-based provision organised along industrial lines. Of course, these systems represent only 'ideal-types': in practice most Beveridgean systems have established a regulatory environment around private pension provision, and most Bismarkian systems have introduced pension entitlements funded directly by the state.

Yet there is also bifurcation within these ideal-types. Pension systems within both models may be more or less redistributive, more or less contributory, and ultimately, more or less generous.

Mehmen Aysan and Roderic Beaujot (2009) refer therefore to four types of European pension systems, influenced by geography as well as philosophy: liberal and social democratic (broadly speaking, variants of the Beveridgean model), continental and Southern (broadly speaking, variants of the Bismarckian model).

The liberal welfare regime, in general, is distinguished by the dominant role of the market in the management of social risks with lower responsibility on the part of the state and the family. Individuals are therefore expected to provide for their own retirement income, traditionally through remuneration arrangements with their employer. The social democratic regime is a variant of the Beveridgean system but places greater emphasis on the state as a provider of pensions, albeit based on economic contributions, through social insurance.

The Southern European regime has a limited role for both state and market, and instead relies mainly on the family to provide old age support. The continental regime – which is the most common in Western Europe – has a similar emphasis on the family, but also encompasses a significant role for the state in organising and funding pension provision, although its basis in existing industrial and occupational roles means it lacks the redistributive mechanisms evident in the social democratic regime.

Crucially, according to Aysan and Beaujot, the process of pensions reform in different countries has been shaped by the parameters established by their traditional pensions regime.

Reform in the liberal regime has focused on containing the cost of pensions to both the state and employers, broadly within existing practices, although new measures to address pensioner poverty have also been introduced to counter some of the worst effects of reform.

The social democratic regime has maintained the state's role in providing pensions, but sought to contain the fiscal burden on the state through moves towards 'defined contribution' rather than 'defined benefit' in state provision, mirroring a similar transition within *private* provision in the classic Beveridge model.

The continental and Southern regimes largely maintained the basic components of their existing practices, although sought to increase working-age contributions towards pension accruals, and restrict entitlement to pensioner benefits in some ways. As a consequence of these reforms, some continental countries have seen the development of private pension provision.

It is worth examining the pensions reform of particular countries in more detail. Reforms can generally be interpreted in terms of the expansion or emergence of different 'pillars', based on the World Bank's seminal 1994 study, which outlined the three pillars of any pensions system:

- A first pillar of state provision: usually, but not necessarily, contributory. It is also universal, in terms of coverage if not in terms of levels of entitlement. The first pillar is usually tax-financed and unfunded.
- A second pillar of mandatory saving: normally funded by individual and employer contributions (whether defined contribution or defined benefit).
- A third pillar of voluntary saving: normally funded only by individual contributions (see World Bank, 1994).

Although the UK experience is usually thought to have been highly influential on the World Bank's intervention, the UK system is unusual in that it has highly developed private pension provision involving individual saving and employer contributions (encompassing additional support and protection from the state) which is in fact traditionally unfunded, and voluntary.

**Sweden**

The reform of Sweden's pensions system, archetypal of a social democratic regime, has been particularly comprehensive. It has transformed its first pillar provision from defined benefit to 'notional defined contribution' (NDC). The reforms, initiated in 1998, mean that the state maintains its role in providing generous pensions, but outcomes will be more closely linked to contributions. Sweden also introduced an additional pillar composed of funded individual accounts, with a straightforward defined contribution design. The state enabled individuals to make a pro-active choice between several investment strategies (Sunden, 2006).

## Italy

Reform of the Italian pensions system, embodying elements of both the continental and Southern European regime, has actually chosen a similar path to Sweden. Although unlike Sweden the system remains grounded in occupational and industrial roles. Italy has adopted a NDC model in place of its first pillar, defined benefit provision – like Sweden, the first pillar remains unfunded but it is hoped that in tying the system to actual contributions, the system will be more sustainable fiscally. The shift towards NDC actually began before Sweden, in 1995, under the 'Dino reforms'. Italy's reform process, however, has been slow – it has lacked the political consensus evident in Sweden. Private pension provision has also been slow to emerge in Italy, although it has recently begun to attract government support (Arza, 2008; Moscarola & Fornero, 2009).

## France

Pension reform in France began in the 1980s, with attempts to increase contributions and restrict benefits within the unfunded first pillar – this process continued under former president Nicolas Sarkozy. France has also sought, however, to introduce additional pillars. Following various incremental measures, the *Plan d'épargne retraite collective* (PERCO) was introduced in 2003, replacing various innovations with salary-saving and profit-sharing schemes with a fully-funded, voluntary pension saving scheme (Natali, 2008). Perhaps the most interesting thing about the French reforms is that they are intimately associated – and were sold as such by policymakers – with the country's efforts to modernise its economy in accordance with global economic change. The reforms were instrumental in 'contributing to the development of French financial and capital markets and thus boosting investment for firms' (Natali, 2008: 117). According to Adam Dixon (2008), pensions reform in France is explained as much by globalisation as it is by population ageing.

### Spain

The Spanish pensions system, fairly typical of a Southern European regime, has also been undergoing reform since the 1980s, with the principal objective of tightening eligibility for first pillar pensions. Yet it has probably moved more decisively away from its Bismarckian origins than similar countries, by establishing non-contributory pensions to guarantee a minimum level of income. Fiscal incentives designed to encourage private pensions provision have also been introduced. Sebastian Sarasa (2008) argues that the risk of poverty among older people has increased in Spain due to pensions reform, but principally due to how state pensions are uprated rather than an increased reliance on private provision.

### C&EE

The most dramatic pensions reforms have been witnessed in Central and Eastern European countries, many of which have undertaken reform as part of the much wider transition from communism to liberal democracy. Poland has replaced its unfunded, defined benefit system with a multi-tier first pillar, with a means-tested minimum income guarantee (like the liberal regime), an unfunded NDC system (like modernising social democratic countries such as Sweden), and a system of funded, individual defined contribution accounts with *mandatory* saving. Despite the multi-faceted nature of Poland's new first pillar, the country has also seen the development of second and third pillar provision in the private sphere (Natali, 2008).

It is worth noting that Central and Eastern Europe is ageing faster that Western Europe. In the EU-15, 33% of the population will be aged 60 or over by 2050. The figure for Eastern Europe is 36%, and within this, 38% for Central Europe (Cerami, 2011). There have been important differences between Central and Eastern Europe in terms of system design, but in general all – with the partial exception of Bosnia and Herzegovina – have introduced three-pillar systems. Mitchell Orenstein's study, however, suggests that globalisation (as transmitted through the process of European integration) was a more important cause of the general move towards privatisation than demographic change.

According to Orenstein, accession to the EU for the countries of Central and Eastern Europe enabled them to gain access to global capital markets. Subsequently they 'out-liberalised' Western Europe, in terms of pensions privatisation, in order to gain a competitive labour market advantage over the EU-15. Pension privatisation therefore 'provided Central and Eastern European liberals with an opportunity to signal a good business climate and economic liberalism in an area that has a substantial impact on labour costs'. Crucially, this does not necessarily reduce the cost of pensions provision in the short-term, but established the shared responsibilities of individuals, employers and the state to facilitate longer-term economic development. Responding to ageing was therefore not the principal motivation:

While demographic ageing is no doubt an important background condition explaining the emerging crisis in pension system finance, it provides only a partial explanation for the rapid spread of pension privatisation itself. Pension privatisation is not the most obvious solution to fiscal pressures resulting from demographic ageing. While pension privatisation can help to ameliorate the fiscal effects of an emerging demographic crisis in the long run, in the short and medium run it actually increases pressure on the government budget. This is because, in the transition to a private pension system, the state must continue to pay current pensioners while diverting a part of payroll tax contributions to private, individual accounts. As a result, the government must borrow money to offset these contributions to individual accounts. Yet governments are often expected to respond to short-term, rather than long-term pressures (Orenstein, 2008).

Martin Bohl et al (2011) argue that the success of privatisation in Central and Eastern Europe is related to the level of development in the domestic capital market, given the impact of this market on pension fund performance. The researchers compared Poland and Hungary, the latter of which nationalised its private pension system last year. Both Poland and Hungary have heavily regulated pensions industries – and found that the low liquidity and small size of the Hungarian equity market had contributed to the difficulties experienced following pensions reform.

As such, further liberalisation of financial markets within Europe may be useful to the Hungarian pension system (although perhaps not the Hungarian economy more generally if it leads to capital flight). Jean Chateau et al (2008) make a very similar argument, in endorsing financial liberalisation both within and beyond Europe. Increased capital flows, resulting from the differential pace of ageing between countries, would also ‘modify the impact of ageing’.

# 2. Prospects for retirement saving

The Global Ageing Preparedness Index, produced by the Center for Strategic and International Studies and supported by Prudential, demonstrates the importance of increasing funded pension savings in the context of demographic change. The authors recommend that at least a quarter of retirees' income should come from pensions saving by 2040. Of the eight EU countries studied, only the Netherlands is projected to reach this threshold.[1] This objective is also deemed 'low priority' for the UK, because the proportion of retiree income coming from pension savings will be above 15%. But it is deemed a 'significant priority' for Germany, Italy and Poland, because the proportion will be above 5% but below 15%, and a 'high priority' for France and Spain because the proportion of retirees' income from funded pensions saving will be below 5%.

The main policy lesson identified by the authors is that saving into funded retirement schemes should be mandatory, given that three of the four countries (including non-EU countries) expected to reach the stipulated benchmark have mandatory or quasi-mandatory funded systems, including the Netherlands (Jackson et al, 2010).

Research by Deloitte for Aviva, looking specifically at Europe, develops similar themes. In assessing the additional amount that European citizens retiring between 2011 and 2051 would need to save to achieve the OECD standard replacement rate (70% of pre-retirement income), they calculate Europe's *annual* 'pensions gap' as €19 trillion. This is equivalent to almost 20% of the EU's 2010 GDP (Aviva & Deloitte, 2012). Disaggregated to the individual level, UK citizens retiring between 2011 and 2051 will need to save an additional €12,300 each year – higher than citizens of any other country, given the UK's reliance of private pensions saving. For Germany, the figure is €11,600 per year, for Ireland it is €9,100, and in France individuals will need to save an additional €7,900 each year before retirement.

The research also included a consumer survey on attitudes to retirement among individuals in the UK, Ireland, France, Italy, Spain and Poland. Only in the UK and Ireland do a substantial number of people, around a third, expect 'a pension plan from a financial provider' to be their main source of income in retirement. The proportion reporting this expectation in Italy is only 9%, and only 15% in France – although 28% in France and 20% in Italy will rely instead upon 'regular saving for retirement' (compared to only 13% in the UK and 15% in Ireland with this expectation). 41% of individuals in Spain, and 45% in Poland, expect state pensions to be their main source of income in retirement – around double the proportion of the other countries surveyed.

Sweden's experience of pensions reform may be illustrative here. Although the move to a NDC model in first-pillar provision has been deemed successful, and popular, Sweden has struggled to instil a savings habit in relation to supplementary, funded saving. Individuals are offered a large range of alternative investment strategies in the new second pillar, with the default scheme designed quite conservatively, but the number of individuals making an active choice regarding supplementary provision has fallen dramatically since its initial

[1] The eight EU countries studied are France, Germany, Italy, the Netherlands, Poland, Spain, Sweden and the UK. A further twelve non-EU countries were studied in the Index: Australia, Brazil, Canada, Chile, China, India, Japan, Korea, Mexico, Russia, Switzerland and the United States.

introduction (Sunden, 2006). This underscores the need for well-designed default schemes – and perhaps for the kind of mandatory saving schemes advocated through the Global Ageing Preparedness Index.

Rob Alessia et al (2011) have conducted research for the Network for Studies on Pensions, Ageing and Retirement, which sheds light for the prospects of boosting retirement saving across Europe. Utilising data from the Survey of Health, Ageing and Retirement in Europe – which collects information on the employment and income histories of older workers and retirees across thirteen European countries – the researchers find a partial 'displacement effect' when second- or third-pillar pensions saving schemes are introduced. In their central scenario, every euro of pensions saving is associated with a 47% decline in non-pension wealth. When asked to save more for their own retirement, individuals are re-directing some funds used previously for general saving (which in itself is to be welcomed) but are also re-directing funds from short-term consumption. The latter is optimal if pensions privatisation is to succeed. Alessia et al conclude optimistically that 'the main results suggest that European households will react to reductions in pensions by increasing private savings, although not strong enough to smooth consumption over the life-cycle' (2009: 23).

The researchers also suggest, however, that the displacement effect is more limited for individuals with lower educational attainment. This is partly due to lower levels of financial literacy, but also the greater likelihood of lower earnings over the life-course. Essentially, pensions saving for those with lower educational attainment is re-directed from short-term consumption rather than general saving.

A study of retirement saving across eight European countries (France, Germany, Italy, the Netherlands, Poland, Spain, Sweden and the UK) by Sara Fernández-López et al (2010) also contains some relevant findings. Based on a sample of more than 6,000 individuals, the researchers find that 'there is a significant group of Europeans with little savings for retirement purposes'. However, the main aim of the study is to assess the determinants of saving for retirement. Remarkably, they find that saving behaviour has the same three main determinants across all eight countries:

- Age positively influences retirement savings. The probability of saving for retirement rises with age, reaching a maximum in the mid-to-late 40s to form a U-shaped relationship between age and savings behaviour.
- Financial literacy positively influences retirement savings. Individuals with a higher level of financial knowledge have a greater tendency to save for retirement. The research suggests, in fact, that access to financial knowledge rather than overall level of education, is a more important effect.
- Income positively influences retirement savings. The higher an individual's income, the higher their probability of saving for retirement. As such, 'retirement planning is least pursued by those who need it most, particularly the economically disadvantaged'.

There is of course a fourth main determinant: the impact of country-level institutional factors, or in more simple terms, nationality. Therefore, 'living in a country with mandatory or a long tradition of private pension plans (such as Sweden and the UK) has a positive effect on saving for retirement. On the other hand, living in France or Italy, where public pension systems still play a major role in the individual's pension benefits, has a negative influence on saving for retirement'.

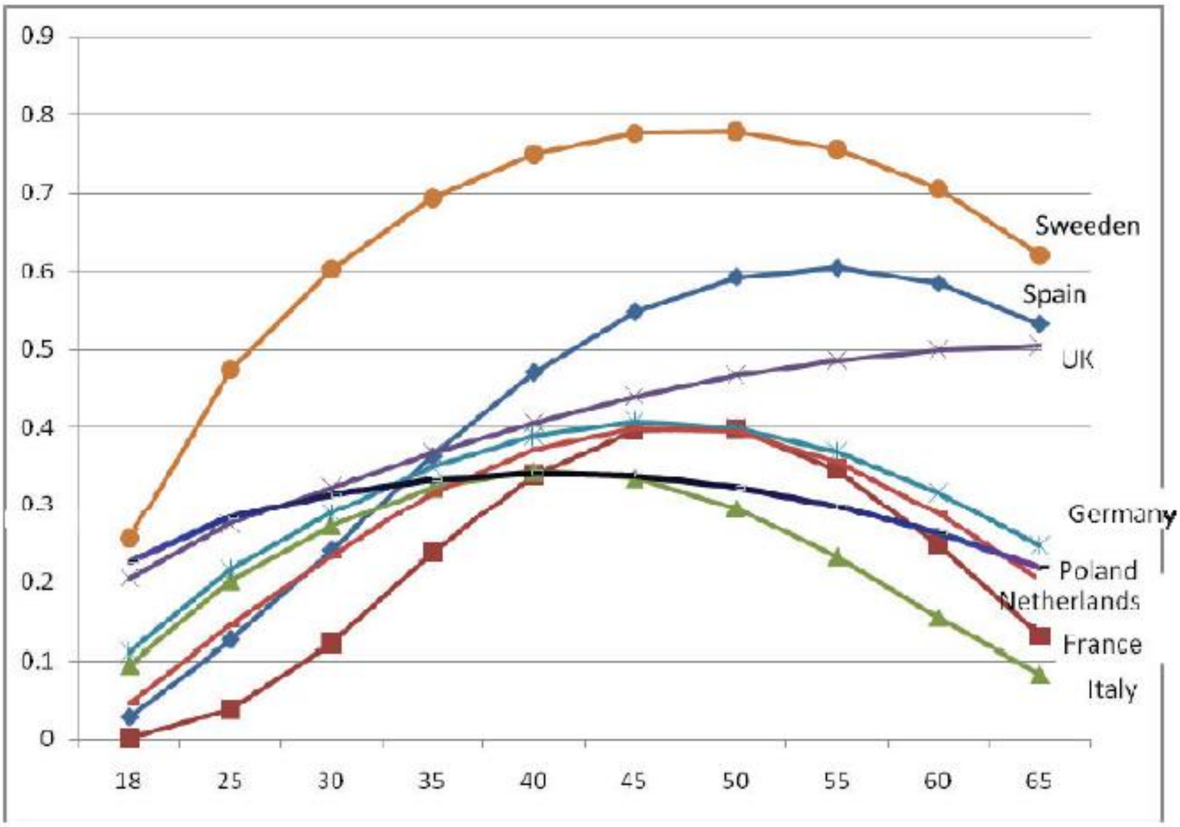


***Fig 1 Probability of saving for retirement by age and country***

*Source: Fernández-López et al, 2010*

Figure 1 therefore shows that, although eight countries appear to have a U-shaped age distribution in terms of probability of saving for retirement, the countries differ significantly in terms of probability profiles across the age distribution (although it does not tell us about the amount being saved).

However, it is hugely significant that, despite the impact of national traditions on retirement saving, age, income and financial literacy affect savings behaviour in all European countries, albeit mitigated by national-level practices and institutions. It suggests that individuals will be able to adapt, and increase their savings level, if these practices and institutions are reformed.

Of course, the financial crisis has undermined the move towards private pensions to some extent. As Mervyn Kohler (2012) argues, through the impact on interest rates and sovereign borrowing, the economic downturn has 'played havoc' with second-pillar provision just as it was becoming embedded across Europe. Both Nick Barr and Peter Diamond (2008), and the International Labour Organisation (2009), have argued that traditional pay-as-you-go pension systems will be affected by the current crisis less than private pension funds, because of their broader diversification of public risks and responsibilities.

Gary Burtless' (2010) work on the 'lessons of the financial crisis' for private pensions provision is worth exploring here. Burtless argues that wide fluctuations in asset returns make it hard for well-informed savers to select a saving rate or a sensible investment strategy for defined contribution pensions; individuals who follow identical investment strategies, but who retire a few years apart, may receive pension outcomes that are significantly different. That said, Burtless argues that the direct impacts of the financial crisis on retirement saving should be minimal for younger cohorts, who are more likely to have most of their retirement outcomes composed of funded pension investments, given that the impact of fluctuations is smoothed over the long-term. The problem is therefore one of the perception that saving is not worthwhile, rather than one of financial loss.

# 3. Where are we now?

Pensions reform has not occurred in isolation across the countries of Europe. It has to some extent been triggered by moves by the EU, or the process of EU accession for the countries of Central and Eastern Europe. More generally, pensions reform has been shaped by the concurrent efforts by policymakers to both protect and harmonise pensions provision within Member States.

## Pension integration

It is generally accepted that a lack of integration among national pensions system – in particular regarding employment-based pensions provision – is a drag on the EU economy (Oomen-Ruijten, 2011). The logic of the European single market suggests that any obstacle to labour mobility, or any obstacle to firms operating efficiently across borders, will be a drag on economic growth.

The first section demonstrated the potential value of financial liberalisation within the EU to private pensions provision across Europe, in enabling access to more developed equity markets. As a corollary to this, the establishment of a single pensions market would also create new efficiencies.

EU policymakers have considered 'portability' of pensions entitlements an important issue, as shown by the proposed Pensions Portability Directive. Until recently, this issue has gone hand-in-hand with the privatisation of pensions provision across the EU. For example, the 2003 Institutions for Occupational Retirement Provision (IORP) Directive sought to ensure that savers do not lose tax relief arrangements for their occupational pension when they work in another EU country.

Another key element of a single pensions market, however, lies in the harmonisation of pensions systems throughout the EU.

It is worth looking at some of the recent EU Directives on pensions provision here. The IORP Directive was EU policymakers' first major, direct intervention in terms of establishing a single pensions market. Its main aims included the development of a common prudential framework and the ability to manage pensions across the EU. It excludes first-pillar provision, but still affects around 25% of the EU labour force. The Directive enabled pension funds in one Member State to manage company schemes in other Member States, and required countries to mutually recognise their regulatory regimes.

The Directive also contained stipulations on the regulation of IORPs, including operational rules and safeguards, and minimum funding requirements (Natali, 2008). Member States were permitted to establish some quantitative restrictions on pension funds, but they have to allow their pension funds to hold up to 70% of their assets in shares and corporate bonds, and to hold at least 30% in non-matching currencies. Member States are not allowed to require prior approval of investment decisions or stipulate investment in a particular category of assets.

In 2005 the European Commission sought to enhance the portability of occupational pensions across Member States through the proposed Pensions Portability Directive, which would establish minimum standards for the acquisition, preservation and transferability of supplementary pension rights. The Directive has not yet been agreed – despite being somewhat diluted in 2007 to remove the transferability elements.

## The White Paper

In 2010 the European Commission issued a Green Paper on pensions policy titled *Towards Adequate, Sustainable and Safe European Pension Systems*. The Commission argued that 'following a decade of reforms that have altered pension systems in most Member States, there is now a need to thoroughly review the EU framework'. The document endorsed multi-pillar pensions provision, but stated that the financial crisis 'has revealed that more must be done to improve the efficiency and safety of pension schemes'.

On the impact of the financial crisis on funded pension schemes, the Green Paper states that:

schemes in countries where solvency requirements were lower and asset value losses particularly large also tend to have poorer protection of accrued entitlements and the least flexible mechanisms for burden sharing. As a result, entitlements can be lost and providers inclined to discontinue schemes, since they cannot afford to bring schemes back to solvency (European Commission, 2010).

As a consequence, the Green Paper argued for, firstly, revisiting 'the regulation of funded pension schemes to ensure that they are efficient and remain safe in the wake of major financial crises whilst ensuring regulation is proportionate and does not push employers into insolvency or into abandoning pension schemes'. And secondly, ensuring that 'financial market regulation is effective and intelligent given the growing role of pension funds'.

Finally, the Green Paper discussed the trend towards defined contribution (DC) provision, and away from the type of defined benefit provision that has thus far been the focus of most EU-level regulatory activity. The document acknowledges uncertainty over 'whether current EU regulation is able to cope with the shift towards DC schemes'. It suggests regulation might be required on both the accumulation and decumulation phases of defined contribution pensions saving, and that design elements such as minimum return guarantees, life-styling portfolio compositions and hybrid schemes might be preferable to current arrangements.

The Commission's White Paper was published in February 2012 and included as one of its recommendations the already-underway review of the IORP Directive.

As with the Green Paper, the White Paper's main headline concerned retirement ages. While recognising the limitations of the EU's power in this regard, the White Paper suggested linking retirement ages to gains in life expectancy.

The European Commission 2012 Ageing Report projected that EU life expectancy at birth for males will increase from 76.7 years in 2010 to 84.6 years in 2060 and life expectancy for females will increase from 82.5 years in 2010 to 89.1 years in 2060 (European Economy 2/2012).

The Commission also offered to co-operate with Member States to improve the efficiency and cost-effectiveness of incentives, including better targeting of incentives on individuals who would otherwise not build up adequate pensions, and provide financial support to those wishing to design cost-effective supplementary pension schemes. The White Paper also encouraged Member States to provide better information on individual pension statements to help individuals with their retirement planning.

## IORP Directive

The European Commission sought detailed advice from EIOPA on revising the 2003 IORP Directive. This advice was published in early 2012. In a press release EIOPA stated its intention to move towards

a harmonised, risk- based prudential regime for IORPs. The objective of the regime is to increase the number of pan-European pension funds from its current low level. In addition, the new framework should ensure regulatory consistency between sectors and enhance protection of members and beneficiaries (EIOPA, 2012).

EIOPA has proposed a 'holistic balance sheet' approach for the IORP Directive, which took employer liability and insolvency protection into account. In its response to the European Commission, EIOPA said many national supervisors had already take a holistic balance sheet approach, but a full impact assessment on capital requirements for the revised IORP Directive would need to be undertaken. This was launched in October 2012, following a consultation.

It has also recommended the introduction of a key information document for all defined contribution schemes across Europe.

European Commissioner for Internal Market and Services Michel Barnier announced in June 2012 that the Commission will not publish any proposals on the revised IORP Directive before summer 2013. The proposals had been expected in late 2012 but the delay will allow policymakers to undertake more detailed quantitative impact assessments.

# 4. ‘Boosting Retirement Saving Across Europe’ private policy debate – 18 June 2012

The financial crisis has put pressure on European regulators and individual Member States to find a solution to the lack of pension provision and individual savings across Europe.

The challenge for policymakers and the European financial services industry is how to tackle the challenges of an ageing population, encourage savings, and develop proportionate regulation to ensure pensions are sustainable and attractive.

The panel that convened at the *Boosting Retirement Savings Across Europe* debate organised by the International Longevity Centre-UK and sponsored by Prudential, looked at how these challenges should be addressed.

**Encouraging saving**

In its White Paper the European Commission highlighted the need to increase retirement savings, but the panel noted that encouraging citizens to save into a pension in straitened economic times is a key challenge for Member States.

All panellists agreed first pillar pensions were vital to preventing pensioner poverty and complementary pillar two savings were needed. If Europeans expect to receive the pension replacement levels which they grew accustomed to in the late ‘70s, ‘80s and ‘90s they must work for longer, or build provision through occupational or private pensions.

There was no consensus on whether mandatory retirement saving should be implemented. While mandatory saving decreases the future cost burden on governments, one panellist felt it was not appropriate and called instead for greater acceptance of individuals’ differing risk appetites and saving preferences, which regulators and the financial services industry must enable.

**Sustainability**

To ensure Europeans have confidence in the pension system, it must be sustainable. All pillars are under pressure due to the inability to mitigate risk and absorb shock when markets rise and fall. There was also concern about the cost efficiency of schemes.

In its White Paper the Commission said it wanted to contribute to addressing these problems, although did not promote one type of pension.

Panellists felt that in order for state pensions to be sustainable, the burden of cost should be spread across generations and increased saving into a second pillar pension is needed. Supplementary pensions should not be seen as a luxury, but accessible to all.

One panellist said the concerns about present pension underfunding should not mar views of pensions in the long-term. Although some pension funds are struggling with large deficits now, it is not a reflection on their ability to pay out in the future.

**Longer working lives**

The panellists agreed that in order to ensure sustainability of pension funds, increased state retirement ages are needed.

They also agreed that older people needed to be encouraged to increase their working lives by changing employer attitudes to older workers, providing older employees with relevant skills and removing legal barriers to employment.

One panellist urged the Commission to follow through on its intent to use part of the European social fund set out for 2014-20 to support projects aimed at the employment of older people. The panellists also suggested that raising the state pension age in Member States provides a permanent agenda for the labour market to employ people for longer.

However, panellists disagreed on whether job creation would improve retirement savings. One panellist argued that the policy of creating jobs and economic growth would boost savings as more citizens would have the incomes to save.

However, another panellist argued that increasing jobs would not help low paid workers who have no savings, and called for structural reform and a policy of decreasing budget deficits to ensure younger generations are not burdened by the debts of older workers.

**Pan-European pension**

Tackling the needs of older generations is key to the retirement saving challenge in Europe, but changes in employment patterns in younger generations need to be taken into consideration.

In the context of an increasingly mobile European workforce, the panel discussed the need to improve pension portability.

The panel said an overview of a worker's pension entitlement from pillar one, two and three would provide individuals with a potential pension outcomes and positively reinforce pension saving. However, the panel was realistic that few Member States could deliver this.

It also discussed a pension tracking service that would allow migrating individuals to transport pension savings in one country to another country. Mobility of pensions was seen as a future project that would only apply to new pension pots, as it would be too difficult to move existing pensions.

Tracking and moving pensions are ambitious targets and the panel instead discussed the creation of a European Commission quality mark for pensions, although concerns were raised about the Commission stamping private pensions and whether Member States would allow it to do so.

Panellists agreed that a European definition of a pension would have to be developed prior to a quality mark.

**Regulatory framework**

To improve pension savings the panel recommended the regulatory framework should promote low risk, cost efficient pension arrangements, and integrate pillars one and two.

The panel recommended the Commission align the IORP Directive with other regulation and take into account pensions provided by both commercial providers and those offered via commercial relations.

One panellist suggested introducing a standard minimum pension level, or a pension income protection mechanism, linked to a poverty threshold.

**Solvency II**

The possible application of Solvency II rules to pension funds under the IORP Directive was criticised by two panellists, who suggested that Solvency II would increase pension capital requirements and place a burden on schemes, particularly smaller schemes.

They called for more research to be undertaken on the impact of applying Solvency II to pension funds and recommended it only be applied in a proportionate manner.

# Conclusion

Demographic and economic change demands reform that makes pensions system more sustainable. It is also right that, if individuals are going to be compelled to take greater responsibility for retirement savings, we should consider the safety of the various saving mechanisms available.

It is clear that Europeans need to be saving more. The most urgent task for policymakers at both national and supranational levels is to ensure that appropriate support and incentive structures are in place. 60% of EU citizens have no workplace-based pension – widening access to pensions saving, most realistically through decent defined contribution-based provision, should be the main priority.

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